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Supreme Court of the United States

OCTOBER TERM, 1943.

No. 964.

FIRST NATIONAL BANK IN WEST UNION, WEST VIRGINIA, a Corporation,

Petitioner,

—against—

AMERICAN SURETY COMPANY OF NEW YORK, a Corporation,

Respondent.

BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI.

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The Question Presented.

The interrogatory as stated in the Petition (3) contains so many inaccuracies and omissions that it is impossible fairly to apprise this Court of the issue, further review of which is sought, unless the question is reframed. Paraphrasing the opening sentences of the unanimous opinion of the Circuit Court of Appeals (R. 324), the question may be more fully and precisely stated as follows:

> *Is a bank liable for the loss of funds of a bankrupt estate misappropriated by a trustee in bankruptcy where, although it was not a designated depository of bankruptcy funds, the bank allowed the trustee to deposit in his individual account certain checks belonging to the bankrupt estate and to withdraw the fund so created by checks given (by himself and his wife) for personal purposes?*

It is, therefore, a distorted picture (none the less gross because unwitting) of the controversy, presented and de-

cided below, which is outlined by the Petitioner, particularly in the concluding portion thereof in which it is gratuitously assumed that "the bank admittedly had no knowledge of any misapplication or intended misapplication of the funds by the Trustee, received no benefit from the transaction, and was not conscious of any impropriety in accepting such deposit".

Subsidiary to the principal issue, there were involved in the litigation below, certain preliminary matters the disposition of which was necessary to the decision of the ultimate question. These were briefed and argued *in extenso* and, as presented by this Respondent in its brief to the Circuit Court of Appeals (at pp. 4 and 5) included the following:

1. Should the defendant bank (not being a designated depository for bankruptcy funds) have permitted the trustee to deposit checks, payable to him as trustee in bankruptcy, to his personal account therein?

2. Did the defendant bank have actual or constructive knowledge or notice of the trust character of the aforesaid funds so deposited?

3. Should the defendant bank have thereafter permitted the trustee and his wife to withdraw such funds by personal checks drawn in payment of their personal obligations?

4. Did the defendant bank have actual or constructive knowledge or notice that such funds were being misappropriated?

5. Was the defendant bank entitled to apply the funds of the bankrupt estate in its hands to reimburse itself for the sums which it paid out to the trustee individually or on checks drawn by the trustee and his wife individually for

individual purposes at a time when the trustee had no individual funds of his own in the bank?

6. Was there, in consequence, a misappropriation of such trust funds by the defendant bank, or a misappropriation to which it was a party?

To paraphrase the issue as stated later by the Circuit Court of Appeals, the principal question might be formulated as follows (R. 330-331):

> *Is not a bank (not being a designated depository) accountable as a constructive trustee when it accepts from a trustee in bankruptcy (who by statute and General Order is prohibited from depositing bankruptcy funds therein) funds of the bankruptcy estate with express notice of their bankruptcy trust character and of the trustee's breach of legal duty in so depositing such funds, thereby knowingly assisting in the trustee's breach of his fiduciary duty, and credits such funds to his personal accounts in which there are no other funds and permits him to withdraw such funds by his personal check without countersignature by judge or referee in bankruptcy?*

Contrary to the unwarranted assumption that certain facts and inferences from facts favorable to the Petitioner were admitted, the record shows that the circumstantial as well as direct evidence points to the existence of "knowing assistance" on the part of the Petitioner in the perpetration of the misappropriation. From this factual background and not alone from the form of the deposit did the Court below draw its conclusion that the bank was liable. Thus, Parker, *C. J.*, wrote (R. 325):

> "At the time of this deposit, the trustee had no balance whatever to his credit in his account with the bank and had not such balance for ten days or more. The deposit was not an ordinary one, but was four times as large as any that had theretofore been made in that account and stood out in sharp contrast with the other deposits, which were for very much smaller

sums, only two other deposits in the history of the account being for as much as $1,000.00. On the day following the deposit, he drew a check against it in the sum of $701.00 in repayment of another fund which he had embezzled, and the remainder of the deposit was gradually checked out by checks drawn against it by the trustee and his wife until on December 6, 1937 the credit balance was entirely exhausted. During this period only one deposit had been made in the account, a deposit of $33.80 on September 10th. The cashier of the bank had served in a bank designated as a bankruptcy depository and was familiar with the limitations applying to the deposit and withdrawal of bankruptcy funds."

And again the learned Judge wrote (R. 327-328):

"* * * When to the fact that the checks were payable to the trustee in bankruptcy in his capacity as trustee is added the fact that the deposit was four times as great as any other made by the trustee in the entire history of his account, that the account had been exhausted at the time of the deposit, and that the bank was a small one with only four employees in a rural community, it is impossible to escape the conclusion that the bank had knowledge as well as notice that the deposit consisted of bankruptcy funds, which the trustee had no right to deposit except in an authorized depository. This is virtually admitted by the cashier in the following passage occurring in his testimony * * *."

It thus appears that the Petitioner has been less than careful in dealing with the facts and with the record when in the question presented to this Court it gratuitously assumes that "the bank admittedly * * * was not conscious of any impropriety in accepting such deposit". Other inaccuracies might also be cited. And while the Petitioner argues that the Circuit Court of Appeals based its reversal on a "very narrow ground" (Petition 11) it fails to refer to the other grounds, independent as well as supplemental, with which the record is replete and upon which it might have predicated its disaffirmance. In this,

and in their over-simplification of the issues in general, the Petitioner's counsel are doubtlessly moved by their desire to persuade this Court to take up a case which is barren of novelty and devoid of "national significance and importance". If the facts are examined and not taken for granted, they will be found adequate to support the decision of the Circuit Court of Appeals; and if the decision is interpreted in the light of those facts, it will be found to be in accordance with the law and consonant with sound banking practice.

Statement of the Matter Involved.

The Petitioner's account (Petition 4-13) under the above heading requires a supplementary statement of certain facts and considerations which have not been touched upon therein but which are material and relevant in this case and themselves support the decision below.

As pointed out by the Petitioner, the trustee endorsed the checks deposited by him in his capacity as trustee in bankruptcy. *He did not endorse them individually.* This is important because it constitutes one of the material points of distinction from *Rodgers* v. *Bankers National Bank,* 179 Minn. 197, 229 N. W. 90, relied upon by the Petitioner (Petition 15-16, 20, 35-36). In the *Rodgers* case, checks were endorsed by the payee-trustee, as such, and then by him individually and deposited in his individual account. From this it might be argued that the trustee obtained title to the funds as an individual and that the customary relation of debtor and creditor between him and the bank was then created. In the instant case, however, assuming such a transmutation of legal relationship were possible by the interposition of an individual endorsement before deposit, no such operation occurred here and the trust moneys remained trust moneys. Hence, it follows that when the Petitioner honored the

individual checks of Ware (the trustee) at a time when he had no money of his own in the bank, the latter was extending personal credit or allowing an overdraft. Ware having failed to reimburse the bank for the advancement, it follows that the Petitioner had no right to seize the trust funds for the purpose of recouping its loss, thereby deriving a benefit.

United States Fidelity & Guaranty Co. v. *Hood*, 122 W. Va. 157.

In the disbursement of the funds of the bankrupt estate the bank was as willing and as knowledgeable a functionary as when it received the deposit in the first place contrary to law. Just as it has been shown and testified to that the bank lent itself to Ware's machinations by taking the deposit in the first instance only because it trusted Ware, so only because it had faith in Ware's fundamental honesty *or* because it felt he could make good any loss the bank might suffer in consequence of the joint venture, did the Petitioner honor his checks regardless of to whom they were drawn and for what purpose. This the bank would not have done, as the cashier said, for anyone but Ware or a person occupying a similar status (R. 142). Thus, the bank had guilty knowledge. It need not have taken any chance at all because not being a designated depository it should not have accepted the deposit at the outset. And if it could have lawfully accepted bankruptcy funds, it should not have honored the trustee's checks without the counter-signature called for by a beneficent law the purpose of which was to protect the bankrupt's creditors and the bank alike.

In paying out the money as in receiving it, the bank acted at a peril known to it and took chances the consequences of which it was aware. Otherwise, there would have been no point in the bank employees' repeated dec-

larations of the faith they had in Ware at the time they dealt with him (R. 142, 144).

The immunity from inquiry enjoyed by Ware apparently extended to his wife who not only drew against trust funds deposited by her husband but did so without the requirement of any power of attorney, an elementary precaution called for by the most casual and trusting of banking institutions (R. 133, 153, 181).

The important and legally significant fact is that the Petitioner knew that not a dollar of the trust moneys which it freely paid out until the fund was exhausted was employed for aught than the trustee's personal purposes or those of his wife (R. 137, 138, 140-142, 185-186).

Detailed examination of the checks themselves (R. 266, 304) serves but to confirm the testimony of the Petitioner's cashier that they bore no marks indicating that they were employed for other than Ware's benefit and that of his wife. From this the bank's employees correctly assumed, as they stated, that the money was being used for personal purposes. A trustee in bankruptcy ordinarily draws checks only to pay administrative expenses and claims of creditors. No checks of this character, it is conceded, were drawn upon the account in question by Ware (R. 157). Moreover, the checks on their face and the manner of their handling by Ware and his wife clearly show now, and clearly indicated to the Petitioner then, that the proceeds were not used and were never intended to be used for fiduciary purposes but were used to pay the obligations of Ware and his wife or went into their pockets. It would be fruitless and serve no purpose here to consider and analyze each of the checks so drawn in order to show what the Petitioner's witnesses have admitted on the trial by way of supplementing and implementing the stipulation of facts (R. 58-68) which alone is sufficient to justify judgment against the bank. But it is nevertheless interesting and not a little shocking to run through the vouchers and observe the manner in which Ware, with the bank's knowledge and assist-

ance, gnawed, pecked and nibbled at the corpus of the trust until nothing but an empty shell was left for the creditors. The quantity of checks, the smallness of many of the amounts, the number payable to cash, the repeated use of the same payee and the names and businesses of the several payees, all well known to everybody in that small community, are as informative and significant to the stranger as they were to the bank on the question of how the money was used. The mute testimony of the books and documents recording this transaction or series of transactions from beginning to end is as revealing as the express stipulation of counsel and the declarations of the witnesses and as eloquently cried aloud for correction not only in the interest of the bankrupt's creditors but of the bank's depositors whose interests were jeopardized by a practice which, it is understood, has now been discontinued by the Petitioner.

Even if the Petitioner had not known throughout the course of these transactions just what was happening there were numerous signs right from the outset pointing to Ware's misappropriations and at least technical faithlessness to the trust which he shared with the bank. For example—a trustee performing his fiduciary duties does not use the local drugstore as a place to cash numerous checks—he does not draw a great many checks to the order of "cash" ranging in sums from one dollar up (R. 304-306)—he does not throw open his account to the use and for the accommodation of his wife. Since the bank knew all this as a joint participant in Ware's activities, the function of inquiry meant little, because even if exercised, it would have added virtually nothing to that of which the Petitioner was already aware.

Nor was it exactly a matter of the bank's closing its eyes to a state of affairs which would have put another institution on guard, because the scene was one which was regarded by this Petitioner with the utmost complacency and even satisfaction. In other words, it was a matter of absolute indifference to the bank what Ware

did with the money, whether he paid his own creditors, whether he used it for pocket money or whether he put it at his wife's disposal. All this is in the record. It stands uncontroverted. The impeachment of irregularity is admitted. In fact, this is the bank's own story of how and where the money went (R. 139-141).

All of the foregoing would be entirely incredible and incapable of rationalization were it not for the fact that the bank itself, by a spurious plea of confession and avoidance, offered an explanation and an excuse, not a good excuse or even a satisfactory excuse and certainly not a legal excuse, namely, that Ware was a responsible man and a prominent and prosperous lawyer (R. 172, 193, 195).

It is respectfully submitted that this might have been sound banking judgment and justification for extending a line of credit to Ware personally—which is what the bank in effect did—but the bank had no right, on Ware's failure, to reimburse itself from the funds of the bankruptcy estate upon which it had laid illegal hands with the help of Ware in the first instance. Nor, to put it another way, did the bank have any right to disburse the estate moneys regardless—on the strength of Ware's personal ability to make good out of his own resources if the bank should be called to account—as it now is. Nor, to put it still another way, did the bank have a right to accommodate what seemed to be a favored and valued customer on any basis other than at its own risk and assumption of loss, if it turned out, as it did, that the bank had misplaced its trust.

Grounds Relied Upon for Allowance of Writ of Certiorari.

The Petitioner seems to present a feigned issue between the West Virginia law as applied by the District Court and the Federal law as applied by the Circuit Court of Appeals (Petition 18).

To be sure, the District Court did say that the Petitioner's liability must be tested by the law of West Virginia (R. 84). But it did not say that the law of West Virginia was contrary to the Federal law or to the general rule.

And the Circuit Court of Appeals did say (R. 331): "In determining the liability of a bank for a deposit of bankruptcy funds made in violation of the terms of the bankruptcy act, however, we do not understand that we are bound by decisions of the local courts; for the question involved is one of federal rather than of local law" (citing cases). But that Court also said (R. 331):

> "We find nothing in the law of West Virginia opposed to the rule which imposes liability as constructive trustee upon a bank which knowingly accepts a deposit that the depositor is forbidden by law to make with it. On the contrary, the general rule seems well settled in West Virginia that one who receives a trust fund with notice that he is not entitled to receive it, is liable to account therefor. * * * We do not understand that under the law of West Virginia a bank which has thus assisted in a misappropriation of funds can escape liability merely because it did not know that the trustee intended to steal them. If, therefore, we were bound by the West Virginia decisions in determining the liability of the bank, we would entertain no doubt as to its liability for the deposit."

Upon the facts as stated hereinbefore, judgment should go against the Petitioner in any court. The Petitioner has not shown in what forum or under what judicial system any different rule would apply. It is unable to bring this case within the purview of any part of Section 5 of Rule 38 of this Court.

I.

The Circuit Court of Appeals was correct in holding that the Federal law governs.

This point is fully and completely dealt with in the opinion below (R. 331-333) wherein Judge Parker wrote:

> "In determining the liability of a bank for a deposit of bankruptcy funds made in violation of the terms of the bankruptcy act, however, we do not understand that we are bound by decisions of the local courts; for the question involved is one of federal rather than of local law. *Clearfield Trust Co.* v. *United States* 318 U. S. 363; *Sola Electric Co.* v. *Jefferson Electric Co.* 317 U. S. 173; *D'Oench, Duhme & Co.* v. *F. D. I. C.* 315 U. S. 447; *Deitrick* v. *Greaney* 309 U. S. 190; *Barnes Coal Corp.* v. *Retail Coal Merchants Ass'n* 4 Cir. 128 F 2d 645; *Cannon* v. *Dixon* 4 Cir. 115 F. 2d 913.
>
> "Directly in point, we think, is the very recent decision of the Supreme Court in *Clearfield Trust Co.* v. *United States, supra.* In that case the question involved was the liability of a bank upon its indorsement of a government check which it had taken upon the forged indorsement of the name of the payee. The defense was that the bank was discharged of liability under local law because of delay of the United States in giving notice of the forgery. In holding the bank liable, the Supreme Court said:
>
> > 'We agree with the Circuit Court of Appeals that the rule of *Erie R. Co.* v. *Tompkins*, 304 U. S. 64, does not apply to this action. The rights and duties of the United States on commercial paper which it issues are governed by federal rather than local law. When the United States disburses its funds or pays its debts, it is exercising a constitutional function or power. This check was issued for services performed under the Federal Emergency Relief Act of 1935, 49 Stat. 115. The authority to issue the check had its origin in the Constitution and the statutes of the United States and was in no way dependent on the laws of Pennsylvania or of any other state. Cf. *Board of Commissioners*

v. *United States* 308 U. S. 343; *Royal Indemnity Co.* v. *United States* 313 U. S. 289. The duties imposed upon the United States and the rights acquired by it as a result of the issuance find their roots in the same federal sources. Cf. *Deitrick* v. *Greaney* 309 U. S. 190; *D'Oench, Duhme & Co.* v. *Federal Deposit Ins. Corp.* 315 U. S. 447. In absence of an applicable Act of Congress it is for the federal courts to fashion the governing rule of law according to their own standards.'

"The control of bankruptcy funds, like the right of the federal government to issue checks, is based upon the Constitution and laws of the United States. The rights and liabilities with respect to the handling of such funds 'find their roots in the same federal sources'; and 'in the absence of an applicable Act of Congress it is for the federal courts to fashion the governing rule of law according to their own standards'. If the local law is not to be looked to for the purpose of determining the extent of a bank's liability upon its indorsement of a check issued under federal law, there is no reason why it should be determinative of the bank's liability with respect to a deposit of funds held by a trustee in bankruptcy for administration under that law. In both cases the bank is dealing with a subject matter controlled by federal law; and in both cases there is the same reason why federal and not local law should determine its rights and obligations."

After discussing *Sola Electric Co.* v. *Jefferson Electric Co., supra,* Judge Parker stated:

"* * * A federal statute here requires the deposit of bankruptcy funds in a designated depository. A deposit elsewhere is violative of the statute; and the consequences flowing from such violation would seem clearly to be 'federal questions, the answers to which are to be derived from the statute and the federal policy which it has adopted'" (R. 334).

The Court also discussed *Dietrick* v. *Greaney, supra,* and concluded on this point:

"On like principles it is clear that a 'federal not a

> state question' is involved in the determination of the legal consequences which flow from a bank's accepting a deposit of bankruptcy funds made in contravention of the provisions of the bankruptcy act" (R. 334).

It is noteworthy that the Petitioner under this point has not referred to the discussion of the Court below or the authorities mentioned therein.

II.

No conflict exists among the Circuit Courts of Appeals requiring review of the instant case by this Court.

The Petitioner has sought to put the decision below in conflict with the holdings in *In re Bogena & Williams* (Seventh Cir.), 76 F. (2d) 950, and *Irving Trust Company* v. *United States* (Sixth Cir.), 83 F. (2) 20 (Petition 24-31). These determinations were duly noted by the Circuit Court of Appeals but it "did not think that they should control our decision here" (R. 329). While some disagreement was expressed with the reasoning in the cases cited, the situations were also distinguishable on their facts. As stated by the Circuit Court of Appeals (R. 329):

> "* * * They were concerned, not with the liability of the bank to the bankrupt estate, but with the right of the estate to preferential treatment in distribution of assets of banks which had become insolvent, and the effect of the decisions was to place the claims of the bankrupt estates on an equal basis with the other depositors * * *."

Each case, we respectfully reiterate, should be viewed in the light of its particular facts and surrounding circumstances. What appear to be conflicts in principle dissolve. *In re Potell*, 53 F. (2d) 877, is particularly pertinent. In this case a bankruptcy receiver deposited estate funds in a bank not designated as a depository. It

was held that the bank must return the money to the bankruptcy receiver. Speaking of Section 61 of the Bankruptcy Act of July 1, 1898 and General Order in Bankruptcy No. 29 the Court in that case said (p. 879):

"That Congress considered these provisions essential to the proper and safe custody of the funds of a bankrupt estate is evident not only from the law as expressed but from the nature of the deposits. The effect thereof is certainly to 'prohibit' the depositing and reception of such funds in and by unauthorized depositories.

"It is plain therefore, that the said receiver in bankruptcy had no right to deposit money of the bankrupt estate contrary to the above provisions of the laws and rules. That whether or not a bank was a designated depository was easily ascertained and a public record. That the officers of the bank knew or should have known that it was not a designated depository. They knew or should have known that they had not even presented nor had filed the bond without which no designation would be made.

"Thus, we came to the question: In whom was the title to this money so unlawfully deposited? The title was not in the bankrupt, for he had been duly adjudicated. It was concededly a part of the bankrupt's estate applicable to the payment of creditors. It was not in the receiver of bankruptcy for he is a mere custodian of such estate. There was no trustee and is none today. This money pending the presence of a qualified trustee, was in the custody of the Court. (Cases cited.)

"Such funds in the temporary possession of a receiver in bankruptcy and held by him in trust as such custodian, and a bank unlawfully receiving such money with full knowledge of the peculiar character of the deposit and in opening a prohibited account with such receiver received it impressed with such trust. The principle in *Allen* v. *United St tes,* 285 F. 678 (C. C. A. 1st), seems applicable."

III.

The trust character of the funds received by the Petitioner and not their "public" or "private" status is controlling on the question of the depository's responsibility.

To sustain a contrary view the Petitioner relies upon *Willoughby* v. *Howard*, 302 U. S. 405 (Petition 31). But, as stated by Mr. Justice Brandeis in his opinion the only question in that case was the following (p. 446):

> "The question for decision is whether a trustee (or receiver) in bankruptcy and the surety on his official bond can be held liable for the loss resulting from the insolvency of the bank in which the estate's funds were deposited, if it was one of the depositories designated by the court under 11 U. S. C. A. §101."

This Court held that the Bankruptcy Act did not in terms relieve the trustee of the common law duty to exercise care in the custody of funds; that the fact that the freedom of choice of the fiduciary is limited by statute does not relieve the trustee of the duty of care and prudence within the field left to his discretion; and that the issue of exercising care in making and maintaining deposits, even if made in a designated depository, should have been submitted to the jury, particularly in view of the personal loans made by the depository to the trustee. In the course of its opinion this Court did point out that the funds of bankrupt estate are private funds as distinguished from federal public funds for which Congress has provided a depository system by which the moneys, as soon as deposited, are in effect in the Treasury of the United States. In this respect, of course, "the provisions in the Bankruptcy Act concerning the appointment of depositories and the deposits to be made by trustees are of a very different character" (*idem*, pp. 453-454). But as the Court below stated (R. 329) "this is a distinc-

tion without a difference". Moreover, the Petitioner not having been a designated depository, it is rather idle to speculate on whether bankruptcy funds which were improperly accepted for deposit therein were "public" or "private" funds since in either case the Petitioner held and dealt with them at its peril.

The case of *Maryland Casualty Company v. Central Trust Company* (New York), 265 App. Div. 416, cited by the Petitioner (Petition 34), is likewise not helpful in the present discussion. There, the Appellate Division (Fourth Department) of the New York Supreme Court merely held (one Justice dissenting) that in a suit by the surety on the trustee's bond based upon the wrongful payment by the defendant bank of checks drawn against funds of a bankrupt estate deposited therewith, where the referee's name had been forged by the trustee in bankruptcy, the pleading by the bank of the usual defenses of due care, and the like, should not be stricken out "unless some other reasons appear to prevent the use of such defenses" (p. 421). Unlike the Petitioner herein, the bank again was a duly designated depository of bankruptcy funds.

Both the District Court (R. 88) and the Petitioner (Petition 16) quote the following statement from the Respondent's brief in the District Court:

> "It is not contended by the plaintiff that there is anything in the Federal statutes, rules and orders which, without more, imposes an absolute liability in the premises upon the defendant * * *."

But neither the District Court nor the Petitioner included in its quotation the sentence following the foregoing which read (Plaintiff's Brief, District Court, 42):

> "* * * By the same token it is highly paradoxical for the defendant to urge that because it was not a designated depository it is exculpated from liability for acts for which it would ordinarily be responsible."

We were not aware that our discussion of this point in the District Court was shrouded in such subtleties that we failed to reach the understanding of that court. Whether or not the Petitioner was a designated depository, and it is conceded that it was not, and whether or not the bank had authority to receive the moneys of bankrupt estates, and it is conceded that it did not, the fact of the matter is that the Petitioner in this instance did receive such moneys and did receive them with express notice and actual knowledge of their trust character which appeared on their face. Whether or not the Petitioner was a statutory depository and whether or not, because of its non-official character, it was absolved from observance of certain administrative rules, the bank was still subject to the ordinary rules of law pertaining to the handling of trust moneys. It is the height of absurdity to contend that because a bank received knowingly and wrongfully, if not unlawfully, funds which it was not eligible to receive and which the trustee was prohibited from depositing therein, it could thereafter handle such money free from all the restraints and restrictions imposed by the familiar rules of common and statutory law in such cases applicable. *Seaboard Surety Co.* v. *State Savings Bank of Ann Arbor* (Mich. Sup. Ct.), 11 N. W. (2d) 321.

We have hitherto adverted to the proposition that the case of *Rodgers* v. *Bankers' National Bank*, 179 Minn. 197, 229 N. W. 90, frequently referred to in the Petition (15, 20, 35), is distinguishable in point of fact from the instant case, in that, among other things, the checks in the *Rodgers* case were endorsed individually by the trustee as well as in his representative or fiduciary capacity. In the case at bar, the trustee did not endorse the checks in an individual capacity. Hence, they came into the bank impressed with the trust clearly labeled on the face and obverse side of each of the eight instruments. The Circuit Court of Appeals has dealt adequately with the

points raised in the *Rodgers* case and the following excerpt from its opinion should, it is submitted, be left as the final word on the subject (R. 330-331):

> "Defendant points to the statement in *Rodgers* v. *National Bank, supra,* to the effect that 'the provisions of the bankruptcy act and the general order mentioned were not meant to regulate the conduct of a bank which is not a designated depository'. This is stating the rule too broadly. It is true, of course, that the provisions of the bankruptcy act and of the general orders in bankruptcy do not apply to a bank which is not a designated depository; but this does not mean that such bank may receive with notice funds which are being deposited in violation of law without taking same as a constructive trustee in accordance with the well settled rule which we have discussed. The statute and general order do not apply to the bank, but they do impose a legal duty upon the trustee in bankruptcy not to deposit the funds therein; and the liability of the bank arises when it receives the funds with notice that they are trust funds and that the trustee is making the deposit in breach of the duty imposed upon him by law. A bank which thus knowingly assists a trustee in the violation of his trust, by allowing him to deposit in his personal account and check out with his personal check funds which he has the right to deposit only in a bonded depository and check out only with a check countersigned by the judge or referee, has no ground to complain when it is held to the liability of a constructive trustee of such funds."

When complaint is made that the rule applied works a hardship on the Petitioner it should be remembered that no extraordinary burden of supervision is placed upon banks handling the estates of bankrupts. Indeed, this burden is substantially assumed by the courts because General Order in Bankruptcy 29 specifically requires the countersignature of a referee in bankruptcy on checks drawn upon bankuptcy funds. To the argument that the Petitioner was not a designated depository the obvious answer is that if such a bank insists upon accepting a prohibited

account it subjects itself to at least the same degree of accountability for supervision, the only difference being that the supervision is unofficial and not judicial but the nature and extent thereof are at least equivalent to that required in the case of other trust estates. As the Circuit Court of Appeals said (R. 328):

> "* * * The safeguards so carefully erected for protecting the deposit and withdrawal of bankruptcy funds would mean little if trustees in bankruptcy were at liberty to disregard them whenever they saw fit to do so, and if banks not authorized as depositories might accept deposits of bankruptcy funds knowing them to be such, credit them to the personal accounts of the trustees and allow them to be withdrawn by the personal checks of the trustees countersigned by no one."

IV.

By failing fully and fairly to apprise this Court of the issues tried and argued below, the Petition attempts to make it appear, contrary to the record, that the judgment is supportable only on a favorable determination of the single issue selected for discussion.

Mention has already been made at the outset that the "question presented" as the basis of the petition for review contains assumptions of admissions allegedly made which are wholly unwarranted. Because the matter goes to the substance upon which the Petition is allowed or denied, we are moved again to advert to the point because of the following statement at the foot of page 11 of the Petition:

> "*Conceding* that the Bank had no knowledge whatsoever of any misapplication of funds by the Trustee, the Court of Appeals based its reversal as to the $4,050.00 item upon this very narrow ground; that * * *." (Emphasis supplied.)

and by the following statement at page 33 of the Petition:

> "* * * The rule of absolute liability applied by the Court of Appeals to Petitioner, in the *admitted* absence of any knowledge on Petitioner's part that the Trustee was misappropriating bankruptcy funds, seems unduly harsh * * *." (Emphasis supplied.)

No such "concession" was made by the Circuit Court of Appeals in respect of the $4,050 item represented by deposited checks. What the Court below said on this point was to summarize the contentions of the respective parties. Thus (R. 335):

> "* * * It is *argued* that the bank should have known from the nature of the checks drawn against the trustee's account that he was misappropriating the funds there deposited; but the officials of the bank *deny* that they knew of the misappropriation or that they paid any attention to the checks drawn by the trustee, assuming that they were properly drawn * * *." (Emphasis supplied.)

In the succeeding sentence of the opinion, which is set out on page 11 of the Petition, the Court speaks of finding no evidence of knowledge on the part of the bank but it is there referring to the item of $793.62 representing checks cashed, not deposited, which matter is not under discussion.

Nor is there any "admitted" absence of knowledge on the Petitioner's part. It must now sufficiently appear to this Court from the record and from this discussion that, beginning with the pleadings and extending throughout the proceedings in the courts below, the issue of the presence or absence of knowledge or notice, actual or constructive, direct or inferential, with respect to *both* the receipt and the disbursement of the funds was the subject of earnest and lengthy argumentation by both parties and of consideration by both courts.

Among other things, it was the contention below of the Respondent, as it is now, that, under the circumstances,

the bank was liable not only because it accepted the deposit but because it permitted its withdrawal in the manner stated, and in support of this proposition references were made to many authorities including the A. L. I. Restatement of the Law of Trusts, particularly Sections 297 and 324. It was also the Respondent's contention then, as it is now, that upon the evidence before the District Court judgment for the Respondent could be sustained upon a selection of legal theories, where a situation involves the responsibility of those whose hands are put upon moneys and whose minds are touched with knowledge of the purpose thereof but whose eyes are averted when the malefactions are committed.

Because of the generality of the rules cited by the Courts below and by opposing counsel and, indeed, by ourselves, it is our submission that while adherence must be had to their enveloping authority, each case must in final analysis be decided on its own circumstances. And this, it is further submitted, is the principal reason why neither justice to the individual nor the public interest will be served by review of the case by this Court.

For the foregoing reasons, it is respectfully submitted that the writ of certiorari prayed for in the Petition to the judgment of the Circuit Court of Appeals for the Fourth Circuit should be denied.

Respectfully submitted,

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